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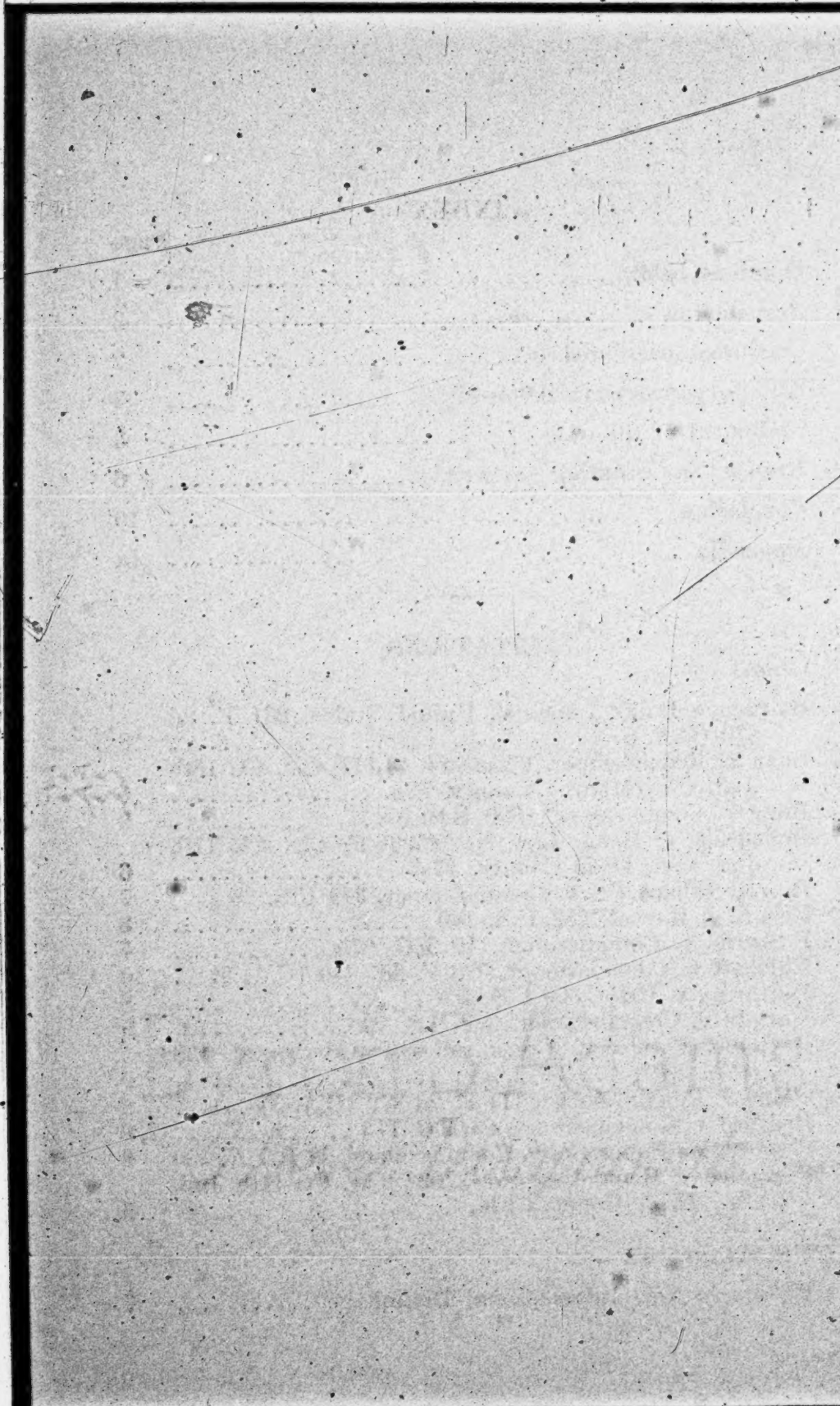

IN THE

Supreme Court of the United States

OCTOBER TERM, 1966

No.

JAMES T. BENN, *Petitioner,*

v.

COMMISSIONER OF INTERNAL REVENUE

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

The petitioner, James T. Benn, respectfully prays that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Fifth Circuit entered in the above-entitled proceeding on October 6, 1966, as amended and reaffirmed on November 15, 1966.

OPINIONS BELOW

The memorandum opinion of the Tax Court is reported at 22 TCM 707 and is reproduced in the Appendix hereto, p. 2a, *infra.*

The per curiam order of the Court of Appeals of October 6, 1966, affirming the judgment of the Tax

Court, is reported at 366 F. 2d 778 and appears in the Appendix hereto, p. 1a, *infra*. The per curiam order of the Court of Appeals of November 15, 1966, denying the petition for rehearing and reaffirming the judgment of the Tax Court, is not yet officially reported; it appears in the Appendix hereto, pp. 1a-2a, *infra*.

JURISDICTION

After a trial ending three years previously, the opinion of the Tax Court was entered on May 31, 1963, and its decision was entered on April 3, 1964. Upon a timely filed petition for review, the Court of Appeals affirmed the Tax Court's judgment on October 6, 1966. Thereafter, on November 15, 1966, the Court of Appeals denied a timely petition for rehearing and reaffirmed the Tax Court's judgment, adding certain comments in so doing. On February 10, 1967, Mr. Justice Black signed an order extending the time for filing this petition for writ of certiorari to and including March 31, 1967. The jurisdiction of this Court is invoked under 28 U.S.C. § 1254 (1).

QUESTIONS PRESENTED

1. Whether, for federal income tax purposes, the delivery of a valid and binding promissory note, one that is both negotiable and interest-bearing, must be considered as part of the cost of acquiring real property, especially where such note is eventually paid.

2. Whether the Tax Court is bound by the decisions of state courts of competent jurisdiction, resolving matters of property rights and interests, in determining issues of fraud and cost of acquired property.

STATUTORY PROVISION INVOLVED

Section 113 (a) of 1939 Internal Revenue Code; Section 1012 of 1954 Internal Revenue Code:

> "The basis of property shall be the cost of such property . . ."

STATEMENT OF THE CASE

After first declaring that the issues in this case "are purely issues of fact" as to which the Tax Court's resolution was proper, the Court of Appeals on rehearing was forced to amend its opinion to read (see Appendix hereto, p. 2a, *infra*):

> "The Tax Court correctly dealt with the legal questions and the mixed questions of law and fact. None of these is of sufficient significance to require an opinion by this Court. All of the remaining issues were purely questions of fact. They were decided by the Tax Court upon evidence which it was entitled to credit. The decision by the Tax Court on these issues is not clearly erroneous, and it is therefore affirmed."

Disregarding the voluminous facts underlying the purely factual issues, this petition presents only those facts relevant to the legal issues here at stake. It is enough to note, by way of background, that the proceedings before the Tax Court involved alleged deficiencies and additions to tax in petitioner's federal income taxes for the years 1951 to 1955, inclusive. Petitioner, a general building contractor, had engaged in the acquisition, holding for investment, and sale of numerous pieces of real estate during those years, out of which developed the various tax issues.

A. The Promissory Notes

In computing petitioner's costs and expenses with regard to most of the properties sold by petitioner during the years in question, the Tax Court included promissory notes given by petitioner in acquisition of the properties only to the extent of their fair market value—which the Tax Court found to be zero. The Tax Court stated that while petitioner in legal theory might be legally liable on these notes, "there appeared to be little likelihood that he would ever pay or could be required to pay them." Appendix, p. 4a, *infra*. In giving these notes to the sellers of those properties, said the Court, petitioner had given "nothing substantially equivalent to cash, and he is not, as a cash-basis taxpayer, to be permitted to deduct as costs or include in his basis any amount for these notes until such time as they are actually paid." Appendix, p. 4a, *infra*.

As indicated by the Tax Court, however, petitioner was legally obligated to pay all these promissory notes. The notes were valid, negotiable and interest-bearing. And, in point of fact, petitioner did eventually pay, prior to the Tax Court trial, all the notes in connection with the transactions challenged by the Court. A determination of the actual cost to petitioner was thus possible in the light of all the relevant facts.

B. The State Court Decisions

In connection with its various findings as to petitioner's tax bases and alleged fraud on his part, the Tax Court made the following determinations:

(1) The Tax Court treated petitioner's cost of acquiring the Stonesthrow Apartments as zero. That property had been exchanged between petitioner and

his ex-wife, Florence M. Redelsheimer, in an attempt to settle their affairs and return themselves to status quo ante, following an annulment of the marriage. As part of that arrangement, petitioner gave his ex-wife a promissory note for $37,500; clearly marked on the reverse side was a notation that petitioner's liability on the note was subject to offsets and liabilities in favor of petitioner against his ex-wife, a condition acknowledged by the ex-wife. These offsets and credits represented money and other property of value given by petitioner to his ex-wife during his marriage and which, as a result of the annulment, petitioner was legally entitled to recover. See Tr. 2127, 2145, 2148.

In disregarding petitioner's offsets, claims and credits against his ex-wife in connection with this note, the Tax Court ignored the Florida state court decree which annulled the marriage. See *Benn* v. *Redelsheimer,* Chancery 13-117, Circuit Court of the Sixteenth Judicial Circuit of the State of Florida in and for Monroe County, dated May 28, 1952. Instead, the court treated the parties as having been divorced and labeled their relationship as bigamous. But had the Tax Court given heed to the annulment decree, wherein the offsets, claims and credits reflected on the back of the Stonesthrow note were recognized as property rights of the petitioner, the cost of acquiring the apartments would have been considered as far in excess of zero.

(2) The Tax Court, sharply critical of petitioner's business practices, labeled as fraudulent a transaction involving a $13,600 note made by one Andy Viglianco —which petitioner allegedly raised in amount from $30.00. In making this finding of forgery, the Tax Court ignored a decision of the Circuit Court of Dade

County, Florida, which accepted the verdict of a jury that such a forgery never occurred. See *Viglianco* v. *Benn, et al.*, Law No. 27028, in the Circuit Court of the Eleventh Judicial Circuit of the State of Florida in and for Dade County. These Florida determinations resulted in a judgment against Viglianco for $13,600, plus costs and interest—totalling $16,930. See Tr. 1737; Exs. 7-G, 35, 36.

(3) The Tax Court further found that petitioner had suffered no loss as a result of a business failure in which petitioner had advanced certain monies, $8000 of which had in turn been advanced by one Dominick Dellaquila. Dellaquila demanded the return of his money from petitioner, who agreed to take over Dellaquila's interest and to give him an $8000 note. Dellaquila sued petitioner on this note and in 1952 obtained a judgment against petitioner in the amount of $8,639.98. See *Dellaquila* v. *Benn,* Law No. 25996-F, in the Circuit Court of the Eleventh Judicial Circuit of the State of Florida in and for Dade County. Petitioner paid this judgment debt in 1955 and reported the item as a bad debt loss for that year. The Tax Court disallowed the loss. See Tr. 1604, 1608, 1642-1651.

REASONS FOR GRANTING THE WRIT

1. An important question in the administration of the federal tax laws is raised concerning the use of legally binding promissory notes in computing the cost of property.

The Tax Court determination, affirmed by the Fifth Circuit, raises a significant problem in the administration of the federal income tax laws—whether and to what extent legally binding and negotiable promissory notes given to acquire property may be used in computing the cost of that property.

That problem finds no ready or definitive answer in the Internal Revenue Code or in the judicial deci-

sions thereunder. The pertinent Code provision (§ 113(a) of the 1939 Code and § 1012 of the 1954 Code) merely states that "The basis of property shall be the cost of such property." This Court has remarked that this language "normally means . . . cost to the taxpayer." *Detroit Edison Co.* v. *Commissioner*, 319 U.S. 98, 102. But as the Tax Court has noted, neither the Code nor the regulations thereunder define the term "cost". *Edwards* v. *Commissioner*, 19 T.C. 275, 279. The Tax Court in that case accordingly adopted a definition of "cost" from Webster's New International Dictionary, defining that word to mean "the amount or equivalent paid, or given, or charged, or engaged to be paid or given for anything bought or taken in barter or for service rendered."

Such a definition is certainly broad enough to cover not only amounts of cash paid by the purchaser of property but also amounts "engaged to be paid" through the issuance of legally binding promissory notes—especially those that are negotiable, interest-bearing and are eventually paid. Such would indeed be the common-sense meaning of "cost" in terms of what the taxpayer actually pays for the properties. And in *Redford* v. *Commissioner*, 28 T.C. 773, the Tax Court followed this common-sense approach and held that a $61,000 promissory note, a note that was negotiable and secured by a first deed of trust, was includable in determining the cost of the property involved.[1]

But the Fifth Circuit's affirmance of the Tax Court action in this case has created further doubt and con-

[1] By a divided vote, however, the Tax Court in *Redford* excluded from the cost determination a second note for $25,000, which was non-interest bearing, non-negotiable and incorporated an agreement whereby the amount due might be less if certain conditions materialized.

fusion in the concept of "cost" by intermingling that concept with notions of allowability of deduction, particularly for bad debts. Citing such decisions as *Eckert* v. *Burnet,* 283 U.S. 140, *Helvering* v. *Price,* 309 U.S. 409, *Baltimore Dairy Lunch* v. *United States,* 231 F. 2d 870 (C.A. 8), and *Quinn* v. *Commissioner,* 111 F. 2d 372 (C.A. 5), the Tax Court here ruled that the promissory notes could not be included in the cost determination until actually paid, petitioner being a cash-basis taxpayer.

But all those cited decisions concerned the allowability of a deduction, especially a bad loss deduction, for payments made in the form of notes in a year prior to the maker being called upon to make good his note. In each case the deduction was disallowed on the tax theory that there is no doctrine of constructive payment equivalent to the doctrine of constructive receipt of income.[2] Obviously, a loss must be ascertainable in the year in which it is claimed as a deduction. But legal commitments in acquisition of property, for purposes of cost determination, involve more careful and sophisticated matters than merely determining how much cash is paid out in any given year. If cost, as this Court said in *Detroit Edison,* means "cost to the taxpayer," it would appear essential to determine the total cost to the taxpayer, including the amounts he is legally obligated to pay and does pay over a period of time by virtue of valid, binding and negotiable promissory notes.

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[2] The Tax Court also cited its prior decisions in *Skaneateles Paper Co.* v. *Commissioner,* 29 B.T.A. 150, and *Redford* v. *Commissioner,* 28 T.C. 773. The *Skaneateles* case involved deductions, not cost determination. The *Redford* case did involve cost determination and permitted a promissory note to be included in the determination; see discussion herein at footnote 1, *supra.*

This intensely practical and obviously recurring tax problem needs exploration by this Court, to the end that the existing confusion may be removed and certainty accorded the concept of cost determination in this context.

2. An important question is raised as to the duty of the Tax Court to recognize and apply state court determinations as to legal rights and interests.

The Tax Court, with the approval of the Fifth Circuit, has made various tax determinations without regard to certain judicial rulings of Florida trial courts of competent jurisdiction. Had those rulings been respected, the Tax Court would have had to revise its findings of fraud and revise its determination that petitioner suffered no loss in the Dellaquila matter. It would have had to recognize that petitioner, as the Florida jury had determined, committed no forgery in the Viglianco matter; it would have had to recognize that the *annulment* of petitioner's marriage involved a state court determination of petitioner's property rights and credits against his ex-wife, as reflected in the Stonesthrow promissory note; and the Tax Court would have had to recognize that the Dellaquila note did involve a bad debt loss.

This Court has already determined that state law "creates legal interests and rights" and that the federal revenue statutes merely "designate what interests or rights, so created, shall be taxed." *Morgan* v. *Commissioner*, 309 U.S. 70, 80. See also *Blair* v. *Commissioner*, 300 U.S. 5, 9-10. As a result, a matter of state law decided by a state tribunal of competent jurisdiction in an adversary proceeding determines the rights of the parties and to that extent is binding and conclusive with respect to the resulting federal tax liabil-

ity. In short, where there is no collusion, the state court litigation is determinative of the legal interests to which federal tax liability attaches. See *Flitcroft* v. *Commissioner*, 328 F. 2d 449 (C.A. 9); *Peyton's Estate* v. *Commissioner*, 323 F. 2d 438 (C.A. 8).

The failure of the Tax Court to respect the non-collusive, pertinent decisions of the Florida courts raises a question of significance in the administration of federal tax justice, a question deserving of consideration by this Court. That court needs to be reminded of its unswerving obligation to respect state court determinations of property rights as to which federal tax consequences ensue.

CONCLUSION

For these various reasons, this petition for writ of certiorari should be granted.

Respectfully submitted,

EUGENE GRESSMAN
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Washington, D. C. 20006
Counsel for Petitioner

March 31, 1967

APPENDIX

IN THE

UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

No. 22332

JAMES T. BENN, *Petitioner,*

v.

COMMISSIONER OF INTERNAL REVENUE, *Respondent.*

Petition for Review of the Decision of the Tax Court of the United States

(October 6, 1966.)

Before TUTTLE, Chief Judge, BROWN and GODBOLD, Circuit Judges.

PER CURIAM: The issues in this case are purely questions of fact. All of such issues having been resolved by the Tax Court upon evidence credited by it, the judgment appealed from is AFFIRMED.

On Petition for Rehearing and Reconsideration

On Petition for Review of Decision of the Tax Court of the United States (Florida Case)

(November 15, 1966.)

Before TUTTLE, Chief Judge, BROWN and GODBOLD, Circuit Judges.

PER CURIAM: The Petition for Rehearing and Reconsideration is DENIED.

This petition complains of the fact that, in its prior decision, this Court stated that all the issues were issues of fact, without commenting upon the mixed issues of law and fact, and the legal determinations of the Tax Court, of which it complains. The opinion by this Court is amended to read as follows:

The Tax Court correctly dealt with the legal questions and the mixed questions of law and fact. None of these is of sufficient significance to require an opinion by this Court. All of the remaining issues purely questions of fact. They were decided by the Tax Court upon evidence which it was entitled to credit. The decision by the Tax Court on these issues is not clearly erroneous, and it is therefore

AFFIRMED.

Judgment

Before TUTTLE, Chief Judge, BROWN and GODBOLD, Circuit Judges.

This cause came on to be heard on the petition of James T. Benn, for review of a decision of the Tax Court of the United States, and was argued by counsel;

ON CONSIDERATION WHEREOF, It is now here ordered, adjudged and decreed by this Court that the decision of the Tax Court in this cause be, and the same is hereby, affirmed.

October 6, 1966

Issued as Mandate: Nov. 23, 1966

TAX COURT OF THE UNITED STATES

Docket No. 78019

JAMES T. BENN, *Petitioner*,

v.

COMMISSIONER OF INTERNAL REVENUE, *Respondent*

Filed May 31, 1963

Opinion

KERN, *Judge:* The transcript of the oral testimony given in the trial of this case exceeds 1,800 pages in length and over 230 exhibits were introduced in evidence at the trial. Thirty-nine witnesses testified.

By a careful reading and rereading of the record herein, our memory has been vividly refreshed with regard to the evidence adduced, to the witnesses who testified (many of whom were rather extraordinary characters), and to the demeanor of these witnesses on the witness stand and their manner in giving testimony.

Most of the transactions involved herein were complex. The complexity of many of them was, in our opinion, due to the manner of doing business deliberately chosen by petitioner for the purpose, *inter alia*, of defrauding those with whom he did business (several of whom were themselves not above duplicity) and also the Internal Revenue Service. The unraveling of these complexities was made more difficult by reason of the fact that with regard to many transactions the testimony of witnesses was in conflict with the testimony of other witnesses. Indeed, in many instances, the testimony of a witness was in conflict with receipts and other documents signed by the same witness, occasionally when purportedly under oath, at prior times. Some of the witnesses impressed us as being guileless and gullible, and some as being both gullible and unscrupulous. In either case, many of them fell victims to petitioner's charm and glibness (assisted in some instances, by their own cupidity).

In the face of these difficulties we have done our best to resolve the troublesome questions of fact presented in this case, and our conclusions (44) as to these questions are set out in our Findings of Fact.

Since most of the issues in this case are factual in character, they are disposed of by our Findings. In our opinion, it would serve no useful purpose to repeat them in this Opinion or to discuss the mass of evidence on which they are based.

However, we do feel that it is advisable to discuss briefly a few matters which present mixed questions of fact and law.

During the years involved herein petitioner was engaged in the business of acquiring and disposing of real and personal property. The purchase price of this property was frequently "paid" partly in cash and partly in petitioner's unsecured promissory notes. He maintained no business office or permanent place of residence. He avoided holding title to property in his own name for any extended period, preferring to immediately dispose of the property, or to have it held in the name of one of his "dummy" corporations or that of Margaret I. Bland. From the attendant circumstances and petitioner's conduct, we have concluded that he affirmatively took steps to impede the collection of his obligations and that he had no intention of honoring certain of the promissory notes for which he acquired property at their maturity or at any other time. While petitioner might have been in theory legally liable on these notes, there appeared to be little likelihood that he would ever pay or could be required to pay them. Accordingly, in computing petitioner's cost and expenses with regard to certain of the properties sold by him during these years, we have included these notes only to the extent of their fair market value, which was zero. In giving these notes to the sellers of those properties petitioner has given nothing substantially equivalent to cash, and he is not, as a cash-basis taxpayer, to be permitted to deduct as costs or include in his basis any amount for these notes until such time as they are actually paid. *Eckert* v. *Burnet*, 283 U.S. 140; *Helvering* v. *Price*, 309 U.S. 409; *Baltimore Dairy Lunch* v. *United States*, 231 F. 2d 870; *Quinn* v. *Commissioner*, 111 F. 2d 372; *Skaneateles Paper Co.*, 29 B.T.A. 150; and *Lloyd H. Redford*, 28 T.C. 773.

In those instances where petitioner borrowed money on his notes executed to third parties and paid the cash proceeds to defray costs and expenses directly to the owner of the property, we have included such payments as part of his basis not-with-standing the nonpayment or uncollectibility of such notes. *Edward W. Edwards*, 19 T.C. 275.

The property sold by petitioner was not held for investment purposes, *Rollingwood Corp.* v. *Commissioner*, 190 F. 2d 263, affirming a Memorandum Opinion of this Court, and it is apparent from the record presented herein that petitioner's modus operandi dictated the immediate sale of property held or acquired by him to customers in the ordinary course of his business. Accordingly, petitioner is not entitled to capital gains treatment on any of the sales in the years involved herein. See *Paul K. Ashby*, 37 T.C. 92; Estate of *Eugene Merrick Webb*, 30 T.C. 1202; *J. Roland Brady*, 25 T.C. 682. Pursuant to the same reasoning, we have also concluded that the loss carryover from 1950 was not a capital loss carryover but was an operating loss carryover.

Respondent contends that a substantial portion of the deficiencies determined for each of the years in issue resulted from petitioner's fraudulent efforts to evade payment of his correct income tax liabilities.

For the years 1951 and 1952, which petitioner contends are closed by the statute of limitations, the burden is on respondent to prove by clear and convincing evidence that petitioner filed for those years false and fraudulent returns with intent to evade tax.

For the years 1951 through 1955, respondent must establish by clear and convincing evidence that some part of the deficiencies determined was due to fraud with intent to evade tax. The fact that for these years the burden of proof with respect to fraud is upon respondent does not relieve the petitioner of his burden of overcoming the presumption of the correctness of the deficiencies in tax for these years as determined by the respondent. See *Snell Isle, Inc.* v. *Commissioner*, 90 F. 2d 481, affirming a Memorandum Opinion of this Court, certiorari denied 302 U.S. 734.

In our opinion the respondent has more than borne the burden of proof imposed upon him with regard to fraud

issued, for all the taxable years, although we have also found that petitioner's understatements of income for the taxable years were in amounts less than those either determined or alleged by respondent.

We have found as a fact that petitioner failed to report a part of his income in each of the taxable years involved herein, that some part of each deficiency was due to fraud with intent to evade tax, and that for the years 1951 and 1952 petitioner's returns were false and fraudulent with intent to evade tax, and that petitioner fraudulently failed to file returns for the years 1953 and 1954. Accordingly, the statute of limitations does not bar the assessment and collection of the deficiencies or additions to tax for the years 1951 and 1952. Since we have found that a part of each deficiency for the taxable years was due to fraud with intent to evade tax, respondent has properly asserted additions to tax pursuant to section 293 (b) of the Internal Revenue Code of 1939 and section 6653 (b) of the Internal Revenue Code of 1954 for each of the taxable years. We have found that petitioner failed to file a Federal income tax return for the year 1953 and petitioner has not shown such failure was due to reasonable cause and not due to willful neglect. Therefore, respondent has properly asserted an addition to tax for this year pursuant to section 291 (a) of the Internal Revenue Code of 1939. Petitioner did not file declarations of estimated tax for the years 1953 and 1954 within the time prescribed by law, and therefore respondent properly imposed the additions to tax pursuant to section 294 (d) (1) (A) of the Internal Revenue Code of 1939. Petitioner has not shown error in respondent's determination that he underpaid his estimated tax for the year 1955, and therefore respondent properly imposed the addition to tax for this year pursuant to section 6654 (a) of the Internal Revenue Code of 1954.

Decision will be entered under Rule 50.

TAX COURT OF THE UNITED STATES

(Caption Omitted)

Decision

Pursuant to the opinion of the Court filed May 31, 1963, and the agreed computation of the tax liabilities filed by the parties; and incorporating herein the facts recited in the computation as the findings of the Court, it is

ORDERED and DECIDED: That there is an overpayment of income tax in the amount of $4,820.41 for the taxable year ended December 31, 1951, which amount was paid after the mailing of the notice of deficiencies;

That there is an overpayment of income tax in the amount of $1,845.40, and an overpayment in the addition to the tax under the provisions of section 293(b) of the Internal Revenue Code of 1939 in the amount of $922.70, for the taxable year ended December 31, 1952, which amounts were paid after the mailing of the notice of deficiencies;

That there are deficiencies in income tax and penalties for the taxable years ended December 31, 1951, 1953, 1954, and 1955, without taking into consideration the jeopardy assessments made in October 1958, as follows:

DEFICIENCIES

		Additions to the tax				
		I.R.C. 1939			I.R.C. 1954	
Year	Income Tax	§ 291(a)	§ 293(b)	§ 294(d)(1)(A)	§ 6653(b)	§ 6654(a)
1951	....	....	$1,276.75	....	....	....
1953	$17,451.66	$4,362.92	8,725.83	$1,737.08		
1954	8,060.69	....	4,030.35	795.27	....	....
1955	52,808.64	....	....	....	$26,404.32	$151.34

That there are no deficiencies in the additions to the tax for the years 1953 and 1954 under the provisions of section 294(d)(2) of the Internal Revenue Code of 1939.

Judge

Entered: April 3, 1964

It is hereby stipulated that the foregoing decision is in accordance with the opinion of the Court and the agreed computation of the parties, and that the Court may enter this decision, without prejudice to the right of either party to contest the correctness of the decision entered herein, pursuant to the statute in such cases made and provided.

Petitioner

SHELDON S. COHEN
Chief Counsel
Internal Revenue Service

In the Supreme Court of the United States

OCTOBER TERM, 1966

No. 1209

JAMES T. BENN, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

MEMORANDUM FOR THE RESPONDENT IN OPPOSITION

Petitioner, during the years in suit, engaged in a large number of complicated business transactions. The Tax Court found that the complexity of these transactions was largely attributable to procedures "deliberately chosen by petitioner for the purpose, *inter alia*, of defrauding those with whom he did business * * * and also the Internal Revenue Service" (Pet. 3a). In the principal transactions here in question petitioner acquired a number of real and per-

sonal properties, usually making a small cash down-payment and giving the seller a note for most of the purchase price. Petitioner then resold these properties without delay. The question before the court was petitioner's cost basis for computing gain on the resale. After an extensive hearing the Tax Court found that petitioner took steps to impede the collection of the notes he had given in purchasing these properties and that he had no intention of ever honoring his notes (Pet. 3a-4a); petitioner does not now challenge this factual finding. Based on these facts the Tax Court concluded that petitioner's cost basis for these properties was limited to the amount he had paid for them in cash and was not increased because of the worthless notes he had given to the sellers (Pet. 3a-4a). The court of appeals affirmed *per curiam* (Pet. 1a-2a).

1. Petitioner argues that his cost basis in the properties should include not only the cash he paid for them, but also his personal notes which he never intended to pay and did not pay.[1] The Code provides that the basis of property for determining gain or loss "shall be the cost of such property." 1954 Code § 1012. This Court has commented that cost in this sense "normally means * * * cost to the taxpayer." *Detroit Edison Co.* v. *Commissioner*, 319 U.S. 98, 102, holding that the taxpayer-utility could not include in its cost basis for certain equipment amounts

[1] Petitioner states that the notes were in fact paid (Pet. 4). This statement is directly contrary to the testimony, including that of petitioner himself (R. 213-218, 223, 258-260, 316, 515-516, 813, 1245-1252, 1509-1510, 1596-1597).

which had been paid by its customers. And where taxpayers have purchased assets subject to liabilities which both parties "anticipated" would never be paid or where taxpayers have assumed, as part of a purchase, "speculative" "contingent" liabilities, the courts have refused to permit them to increase their cost basis to reflect such liabilities. *Columbus & Greenville Railway Co.* v. *Commissioner*, 42 T.C. 834, affirmed, 358 F. 2d 294 (C.A. 5), certiorari denied, 385 U.S. 827; *Albany Car Wheel Co.* v. *Commissioner*, 40 T.C. 831, affirmed *per curiam*, 333 F. 2d 653 (C.A. 2).

Similarly here, where petitioner had no intention of paying and did not pay the notes he had given for the properties, he has incurred no cost because of them and his cost basis should not be increased because of them. Thus, the lower courts correctly held that if petitioner purchased a piece of property for $35,000, paying $5,000 cash and giving his unsecured note (which he had no intention of paying) for the remaining $30,000 and resold the property for $35,000 cash, he would have a gain of $30,000.[2] Therefore, there is no need to explore in this case the ques-

[2] This result is also supported by cases like *James* v. *United States*, 366 U.S. 213 and *Rutkin* v. *United States*, 343 U.S. 130. In those cases the Court held that the proceeds of embezzlement or extortion constitute income even though the taxpayer had an unconditional obligation to make restitution. Similarly, when a taxpayer obtains a piece of property on credit—with no intent to pay for it—and immediately resells the property at a cash gain of $30,000, he has $30,000 of income, just as if he had embezzled property worth $30,000 with no intent to make restitution.

tion argued by petitioner—whether a normal taxpayer on the cash receipts and disbursements method of accounting who acquires property in exchange for a note *which he does intend to pay* can include the note in his cost basis for the property.

2. Petitioner also argues that the instant decision is inconsistent with three adjudications of the lower courts of Florida rendered in adversary proceedings between himself and various individuals. As a factual matter, however, these Florida decisions are completely irrelevant to the question before the federal courts in the instant case.

(a) *The Stonesthrow Apartments.* One of the questions before the Tax Court was the amount of petitioner's gain on sale of the Stonesthrow Apartments. He acquired this property from his ex-wife in exchange for his personal note in the amount of $37,500 (R. 2081-2082). The Tax Court found that petitioner never made any payments on this note and that he never intended to do so; thus it held that his cost basis in the Stonesthrow Apartments was zero (R. 2081-2083). Petitioner apparently argues that he paid the note by offsetting it against amounts which his ex-wife owned him and that the Tax Court was bound by the Florida decree annulling his marriage (Pet. 4-5). But regardless of whether his marriage ended by divorce or annullment, there is nothing in the record to prove that his ex-wife owed him any money which he could offset against his $37,500 note to her, and she testified at trial that she did not owe petitioner any amounts (R. 1582).

(b) *The Viglianco note.* Another question before the Tax Court was the amount of petitioner's gain on the sale of a note for $13,600 signed by one Andy Viglianco. Viglianco testified that he had borrowed $30 from petitioner and given him a note for that amount which petitioner had then raised to $13,600 without authority (R. 2077-2079). Petitioner testified that Viglianco had given him the note for $13,600 in payment of an earlier note (R. 2078). The Tax Court found that the earlier note was executed by Viglianco without any consideration from petitioner and thus that regardless of whether it accepted Viglianco's or petitioner's version, petitioner's cost in acquiring the note did not exceed $30 (R. 2069, 2079).

Petitioner argues that the Tax Court erred in not according weight to a jury verdict in a lawsuit against Viglianco by the ultimate purchaser of the note (Pet. 5-6). The jury found that the note had not been raised in amount and granted the purchaser a judgment against Viglianco for $13,600 plus costs (R. 1734-1737). This verdict is not, however, inconsistent with the Tax Court's holding that petitioner had not proved that he paid Viglianco anything more than $30 for the note.

(c) *The Dellaquila judgment.* Petitioner argues that the Tax Court erred in disallowing a claimed deduction for approximately $8,000 which he claims to have paid to one Dominick Dellaquila in satisfaction of a judgment which Dellaquila obtained against petitioner in a Florida court (Pet. 6). The Tax Court accepted the Florida judgment and denied the

deduction only because it found—contrary to petitioner's statement in the petition (Pet. 6)—that petitioner had not paid the judgment (R. 2101). There is no evidence in the record to the contrary.

The petition for certiorari should be denied.

Respectfully submitted.

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JUNE, 1967.

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SUPREME COURT, U. S.

JUL 7 1967

JOHN F. DAVIS, CLERK

IN THE

Supreme Court of the United States

OCTOBER TERM, 1967

No. 76

JAMES T. BENN, *Petitioner,*

v.

COMMISSIONER OF INTERNAL REVENUE

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit

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PETITIONER'S REPLY BRIEF

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July 7, 1967

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PETITIONER'S REPLY BRIEF

The Commissioner's brief asserts (p. 2) that the Tax Court found that petitioner had no intention of ever honoring any of the promissory notes involved in the cost computation and that the notes were not in fact

paid prior to the Tax Court trial.[1] The Commissioner would thus seek to avoid a resolution of the first question presented in the Petition—whether the delivery of valid and binding promissory notes must be considered as part of the cost of acquiring real property.

But the Commissioner's broad assertion is so belied by the findings of the Tax Court and the record of the proceedings as to render the question most appropriate for consideration. While the Tax Court did say (Pet., p. 4a) that petitioner had no intention of honoring "certain" of the notes and that there appeared to be little likelihood that he would ever pay those "certain" notes, the Tax Court did concede in its findings of fact that many of the other notes involved in this computation were in fact paid. Thus, in speaking of the $65,764.40 spent by the petitioner in acquiring and constructing a motel in Miami, the Tax Court found (R. 2065) that "most of . . . [this] money was borrowed by petitioner from a number of people. Most of the borrowed money [represented by some of the notes in issue] was repaid, although some of the money repaid was later borrowed [after the tax years in question] by petitioner for other purposes."

The record conclusively demonstrates, moreover, that the notes, other than the "certain" ones mentioned

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[1] In summarizing the Tax Court's conclusions, the Commissioner mistakenly states (Br., p. 2) that the court found that "petitioner took steps to impede the collection of the notes he had given in purchasing these properties and that he had no intention of ever honoring his notes." Actually, the court found (Pet., p. 4a) only that "he affirmatively took steps to impede the collection of his obligations and that he had no intention of honoring *certain* of the promissory notes for which he acquired property at their maturity or at any other time." [Emphasis added.]

but not identified in the Tax Court opinion, were in fact paid prior to the trial in 1960. These notes were:

1. The Viglianco note of $27,300, which was marked paid and cancelled in 1950. Ex. LLL.

2. The Viglianco note of $12,500, which was paid and released in 1951. Exs. 10, 17.

3. The Glantz note of $11,000, which was marked paid in 1951. Ex. 22.

4. The Doeber notes of $5,250, and $1,980, both receipted as having been paid in 1951 by renewal notes, which in turn were paid in cash in 1954. Ex. 24, Tr. 504-507, 535-537.

5. The Redmon note of $9,350, which was marked paid "in cash" in 1951. Ex. LL, Tr. 231-A.

6. The Reisen note of $4,500, which was assigned on July 12, 1954, to Wharton for an indebtedness of Reisen to Wharton; petitioner paid $4,500 in cash to Wharton on October 1, 1954. Wharton acknowledged under oath the receipt of this money. Ex. LLLL; Tr. 1328-1329.

7. The Glantz note of $12,000, which was paid in 1954. Ex. 24; Tr. 535-537, 557-559.

The foregoing constitute the notes which were in fact paid by petitioner and which should have been utilized in computing the cost of the properties involved. Yet the Tax Court has lumped these paid notes together with "certain" other notes that were unpaid [2] and enunciated the general principle that none of them was to be used in computing petitioner's costs.

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[2] The Tax Court apparently had in mind the unpaid $37,500 note to Florence Redelsheimer, petitioner's former wife. Petitioner offered to pay off that note as part of the property settlement with her. Tr. 754.

Therein lies the basis of the first question presented by petitioner herein, a question which requires no reassessment of the facts as found by the Tax Court and as revealed by the record.

The confusion evident on the face of the Tax Court's opinion as to the various paid and unpaid notes and its failure to discriminate between them might make it appropriate to remand the case to the Tax Court for further consideration—particularly in light of the Commissioner's refusal to justify the proposition that promissory notes that are paid should be excluded from the cost basis of property. But whatever the disposition, the fact remains that the first question set forth in the petition for certiorari is both appropriate and ripe for consideration by this Court.

The critical question at issue here is whether a taxpayer on a receipt and disbursement method of accounting who acquires property in exchange for notes which he does intend to pay and *which he in fact pays* can include those notes in his cost basis for the property. The Commissioner seemingly concedes that he can; certainly the Commissioner does not argue to the contrary. And the failure of the Tax Court and of the Fifth Circuit to recognize and apply that principle to the plain relevant facts of this case fully warrants corrective action by this Court, particularly in view of the recurring and practical nature of this tax problem.

For these reasons, supplementing those set forth in the Petition, certiorari should be granted.

Respectfully submitted,

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July 7, 1967

In the Supreme Court of the United States

OCTOBER TERM, 1967

No. 76

JAMES T. BENN, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

SUPPLEMENTAL MEMORANDUM FOR THE RESPONDENT

The controversy in this case involves the determinations by the courts below that petitioner's cost basis in certain promissory notes was zero. The Tax Court found that petitioner had in fact no intention of honoring these notes and that he took steps to impede their collection. Petitioner has filed a reply brief in this Court which asserts that the courts below found petitioner's cost basis in notes *which he had in fact paid,* to be, nevertheless, zero. This statement is simply wrong. We are therefore filing this memorandum to refer the Court to the portions of the record that refute the seven specific examples that petitioner has constructed (Reply Br. 3):

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1. *The Viglianco note of $27,300.* There is no issue in this case as to the value of the $27,300 note that petitioner gave Viglianco and paid and had cancelled in 1950. Nor was there any issue as to the fact that petitioner did satisfy it. The issue was as to petitioner's cost basis in the property he transferred to Viglianco in satisfaction of the note. As the Tax Court found, petitioner had no cost basis in that property, and, thus, upon obtaining the cancellation of the note, he realized income in its full amount. (R. 2066–2070.)

2. *The Viglianco notes of $12,500.* The Tax Court properly found (based upon evidence of record involving failure of payment through non-existent Brazilian Cruzeiros) that this note had not been paid (R. 223, 2075–2076).

3. *The Glantz note of $11,000.* The Tax Court found that petitioner paid this note and allowed petitioner the face amount of the note in determining his costs (R. 2072).

4. *The Doeber notes of $5,250 and $1,980.* The Tax Court allowed the full amount of these notes in determining petitioner's cost basis in the Robinson Brick Company (R. 2071, 2072, 2076).

5. *The Redmon note of $9,350.* The Tax Court found on evidence of record that it had not been paid, and that petitioner did not intend to pay it (R. 258–260, 2073–2074).

6. *The Reison note of $4,500.* The Tax Court found the note had not been paid (R. 2090). Petitioner's citation to "Tr. 1328–1329" is in fact to sworn testimony denying that it was ever actually paid (reprinted at R. 1419–1421).

7. The Glantz note of $12,000. The record shows that $8,000 was paid, and that petitioner received full credit in computing his costs (R. 2080, 2093–2094).

The petition for a writ of certiorari should be denied.

Respectfully submitted,

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